

Letter of Findings: 01-20100461
Individual Income Tax
For the Years 2005, 2006, and 2007

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ISSUES

I. Individual Income Tax – Imposition – Non-filer.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-5-2; IC § 6-8.1-5-4; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer protests the imposition of additional income tax.

II. Tax Administration – Underpayment Penalty and Negligence Penalty.

Authority: IC § 6-3-4-4.1; IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer protests the imposition of the underpayment penalty and the negligence penalty.

STATEMENT OF FACTS

Taxpayer is the sole shareholder of an Indiana S corporation, which performed contract services. Pursuant to an audit, the Indiana Department of Revenue ("Department") discovered that the S corporation failed to retain adequate records for the audited years. The Department also found that the S corporation did not file its Indiana corporate income tax returns for tax years 2006 and 2007. The Department's audit, thus, adjusted the S corporation's income based on the best information available at the time of the audit. The audit's adjustment resulted in an increase of corporate net income, which, in turn, passed through to Taxpayer, the shareholder.

Upon reviewing Taxpayer's individual income tax filings, the Department further discovered that Taxpayer did not file his Indiana Individual Income Tax returns for tax years 2005 and 2007. Thus, the Department assessed Taxpayer additional income tax, interest, as well as underpayment and negligence penalties also based on the best information available as a result of the audit.

Taxpayer protested the assessments. A hearing was held. This Letter of Findings ensues. Additional facts will be provided as necessary.

I. Individual Income Tax – Imposition – Non-filer.

DISCUSSION

The Department assessed Taxpayer additional income tax based on the best information available as a result of the audit. Taxpayer asserts that he is not responsible for the Department's proposed assessments because the statute of limitations applies. Taxpayer also maintains that his accountant is responsible for properly filing the returns on his behalf.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

IC § 6-8.1-5-1(b), in pertinent part, states "[i]f the department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department. The amount of the assessment is considered a tax payment not made by the due date and is subject to IC § 6-8.1-10 concerning the imposition of penalties and interest."

IC § 6-8.1-5-2, in relevant part, provides:

Except as otherwise provided in this section, the department may not issue a proposed assessment under section 1 of this chapter more than three (3) years after the latest of the date the return is filed, or either of the following:

(1) The due date of the return.

(2) In the case of a return filed for the state gross retail or use tax, the gasoline tax, the special fuel tax, the motor carrier fuel tax, the oil inspection fee, or the petroleum severance tax, the end of the calendar year which contains the taxable period for which the return is filed.

...

(f) If a person files a fraudulent, unsigned, or substantially blank return, or **if a person does not file a return, there is no time limit within which the department must issue its proposed assessment. (Emphasis added).**

IC § 6-8.1-5-4 further provides:

(a) Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices,

register tapes, receipts, and canceled checks.

(b) A person must retain the books and records described in subsection (a), and any state or federal tax return that the person has filed:

(1) For an unlimited period, if the person fails to file a return or receives notice from the department that the person has filed a suspected fraudulent return, or an unsigned or substantially blank return.

(2) In all other cases, for a period of at least three (3) years after the date the final payment of the particular tax liability was due, unless after an audit, the department consents to earlier destruction.

In addition, if the limitation on assessments provided in section 2 [IC 6-8.1-5-2] of this chapter is extended beyond three (3) years for a particular tax liability, the person must retain the books and records until the assessment period is over.

(c) A person must allow inspection of the books and records and returns by the department or its authorized agents at all reasonable times.

(d) A person must, on request by the department, furnish a copy of any federal returns that he has filed.

After an administrative hearing, Taxpayer was afforded additional time to submit documentation to substantiate his claim. Taxpayer, however, only provided tax returns for tax years 2005 and 2006. The 2005 tax returns were signed by Taxpayer and dated December 6, 2010. Taxpayer's documentation demonstrates that Taxpayer prepared those returns only after the Department conducted the audit in 2010. Taxpayer was a non-filer at the time of the audit for both corporate and individual income tax purposes. Therefore, the statute of limitations does not apply pursuant to IC § 6-8.1-5-2(f). Moreover, Taxpayer's accountant is the agent employed by Taxpayer to ensure his compliance with the Indiana statutes and regulations. Taxpayer, as the principal, is responsible for his agent's compliance failure.

Given the totality of circumstances, in the absence of other documentation, the Department is not able to agree with Taxpayer that he has met the burden demonstrating the Department's proposed assessment is wrong.

FINDING

Taxpayer's protest of the imposition of additional income tax is respectfully denied.

II. Tax Administration – Underpayment Penalty and Negligence Penalty.

DISCUSSION

Taxpayer protests the imposition of the underpayment penalty and the negligence penalty.

A. Underpayment Penalty.

The Department imposed an underpayment penalty because Taxpayer failed to timely remit his estimated payments of adjusted gross income tax pursuant to IC § 6-3-4-4.1.

IC § 6-3-4-4.1, in pertinent part, states:

(a) Any individual required by the Internal Revenue Code to file estimated tax returns and to make payments on account of such estimated tax shall file estimated tax returns and make payments of the tax imposed by this article to the department at the time or times and in the installments as provided by Section 6654 of the Internal Revenue Code. However, the following apply to estimated tax returns filed and payments made under this subsection:

(1) In applying Section 6654 of the Internal Revenue Code for the purposes of this article, "estimated tax" means the amount which the individual estimates as the amount of the adjusted gross income tax imposed by this article for the taxable year, minus the amount which the individual estimates as the sum of any credits against the tax provided by [IC 6-3-3](#).

...

(b) Every individual who has adjusted gross income subject to the tax imposed by this article and from which tax is not withheld under the requirements of section 8 [IC 6-3-4-8] of this chapter shall make a declaration of estimated tax for the taxable year. However, no such declaration shall be required if the estimated tax can reasonably be expected to be less than one thousand dollars (\$1,000). **In the case of an underpayment of the estimated tax as provided in Section 6654 of the Internal Revenue Code, there shall be added to the tax a penalty in an amount prescribed by [IC 6-8.1-10-2.1\(b\)](#). (Emphasis added).**

Taxpayer did not provide sufficient documentation demonstrating that the imposition of the underpayment penalty is not appropriate.

B. Negligence Penalty.

Taxpayer also protests the imposition of the negligence penalty.

Pursuant to IC § 6-8.1-10-2.1(a), the Department may assess a ten (10) percent negligence penalty if the taxpayer:

- (1) fails to file a return for any of the listed taxes;
- (2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment;
- (3) incurs, upon examination by the department, a deficiency that is due to negligence;
- (4) fails to timely remit any tax held in trust for the state; or
- (5) is required to make a payment by electronic funds transfer (as defined in [IC 4-8.1-2-7](#)), overnight courier, or personal delivery and the payment is not received by the department by the due date in funds acceptable

to the department.

[45 IAC 15-11-2](#)(b) further states:

"Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The Department may waive a negligence penalty as provided in [45 IAC 15-11-2](#)(c), in part, as follows:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

In this instance, Taxpayer asserts that his accountant is responsible for the compliance failure. However, as discussed in Part I, Taxpayer's accountant is the agent employed by Taxpayer to ensure his compliance of the Indiana statutes and regulations. Taxpayer, as the principal, is responsible for his agent's compliance failure. Since Taxpayer did not provide sufficient documentation to establish that his failure to pay tax or timely remit tax was due to reasonable cause and not due to negligence. The Department thus is unable to abate the negligence penalty.

FINDING

Taxpayer's protest of the underpayment penalty and the negligence penalty is respectfully denied.

SUMMARY

For the reasons discussed above, Taxpayer's protest of the imposition of additional income tax is respectfully denied. Taxpayer's protest of the underpayment penalty and negligence penalty is also respectfully denied.

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